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SUBJECT: SICHUAN RESEARCHER ON CHALLENGES TO ECONOMIC DEVELOPMENT

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CLASSIFIED BY: James Boughner, Consul General, United States
Consulate, Chengdu.
REASON: 1.4 (b), (d)

¶1. (C) Summary: Sichuan Province, the third largest in China, ranks only tenth in terms of economic development, according to Wang Xiaogang (strictly protect), Deputy Director of the Sichuan Development Research Institute. While the purpose of "Scientific Development" is to bridge the gap between East and West China, the quality of Sichuan's development is "not good enough," and minority regions of the province pale in comparison to non-minority regions. Wang told us that Sichuan cannot compete with China's coastal regions, and that it needs to focus more on development of heavy equipment and power equipment manufacturing, natural resource development, agricultural products and value-added processing of food products, and promotion of high-tech products. One reason for China's fast economic growth is competition between local governments to get ahead. Wang opined the central government should enact better regulations in favor of the environment, energy efficiency, and peoples' livelihoods, including more favorable policies for transfer of funding from wealthy coastal areas to poorer western areas. Even though the investment environment has improved, Sichuan is still ten years behind the coast due to its inland location and transportation infrastructure. The province should nevertheless be able to attract new companies in light of its current very low investment base. End Summary.

¶2. (C) Wang Xiaogang (strictly protect), Deputy Director of the Sichuan Economic Development Research Institute, an institute of the Sichuan Development and Reform Commission, recently met with Washington visitors from the Bureau of Intelligence and Research (INR) and Congenoff. We had a broad-ranging discussion of issues affecting the development of Sichuan Province's economy.

Sichuan: Third in Population,
Tenth in Economic Development

¶3. (C) Wang noted that Sichuan Province is the third largest in the country and that its population is rising. In terms of economic development, however, the province ranks only tenth. Per capita income is RMB 10,000 (USD 1,300) per year, which is 66 percent of the national average of RMB 16,000 (USD 2,105). While there are a lot of natural resources in Sichuan, they are not so abundant when considered on a per capita basis. Wang noted that environmental conditions in Sichuan are important to all of China because of the initial flow of the Yangtze and Yellow Rivers through the province.

"Scientific Development" to Bridge Gap Between East and West

14. (C) Wang opined the quality of Sichuan's development "is not good enough," and the profitability is "not high enough." He said the purpose of the "Scientific Development" concept was to coordinate different economic areas across China. However, in Sichuan, the growth in individual income is not up to the national level, nor is the return on capital or labor, which is 60 percent of the national level. Wang explained the two indexes the government uses to assess economic development: the predictive index -- what is planned/hoped for, and the compulsory index -- what the central government dictates for growth and environmental standards. According to Wang, if the compulsory measures cannot be attained by provincial authorities, the central government will decide that either 1) the provincial government has not tried hard enough, or 2) there were objective reasons why the goals could not be met. Wang added that Wen Jiabao already knows China will not meet the goal of equalizing development, but feels compelled to promote the goal.

Sichuan Urban-Rural Gap Expansive

15. (C) Just as there is a large gap between East and West China, Sichuan has an expansive rural-urban gap. Northeast Sichuan is a good example. Large reserves of natural gas have recently been found there, and within 10 years, there should be 30 billion cubic meters of production. However, the region lacks water, is not economically developed, and has "too many people."

16. (C) Minority regions of Sichuan pale in comparison to non-minority regions, Wang said. Liangshan (an Yi nationality region in the southwest) and Ganze and Aba (Tibetan regions in the west) are all extremely poor. The area of these regions is

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two-thirds of Sichuan's territory, but only seven percent of the population (6 million people) lives there. While the resource per capita ratio is satisfactory, the population quality is low, he asserted. (Note: When Chinese mention "low quality" population, they are generally referring to low education and "cultural" levels. End Note). The minority populations are principally farmers or herders who are not interested in trade, Wang stated. These minority areas do have abundant tourism resources and hydropower capacity amounting to two-thirds of Sichuan's total. Nationally, 20 percent of potential hydropower resources have been exploited, but in Sichuan, only 10 percent have been exploited, so there is still great potential for development of this resource.

Sichuan Cannot Compete with the Coast

17. (C) Wang said Sichuan cannot compete with China's coastal regions. It needs to use its own resources to develop, and it should develop industry. Large state-owned companies in Sichuan include those in the fields of natural gas, steel production, and hydropower. The National Development Reform Commission (NDRC) controls prices in these industries which means profits go to the central government.

Five-Year Plan Targets Development of Industry

18. (C) Wang said the Economic Development Research Institute was involved in the development of Sichuan's 11th Five-Year Plan. In the plan, institute scholars emphasized the development of heavy equipment and power equipment manufacturing, natural resource development including clean energy, agricultural products and value-added processing of food products, and promotion of high-tech products. In addition,

they recommended further development of tourism, creation of a modern services industry, and development of large industrial groups.

¶9. (C) Wang said there was also a New Socialist Countryside project to create a modern agricultural economy. It sets out five economic regions of Sichuan that need to develop scientifically: 1) Chengdu, 2) southern Sichuan, 3) northeast Sichuan (the poorest area), 4) northwest Sichuan, 5) and southeast Sichuan. The Sichuan 11th Five-Year Plan predicts a GDP growth rate during 2006-2010 of nine percent. Wang noted that internally, however, the provincial government thinks it will achieve a ten percent rate.

Local Governments Compete to Get Ahead

¶10. (C) When queried whether China has achieved fast growth because it has taken the market economy route, Wang responded negatively. He pointed out that India also has a market economy and it has not achieved such fast growth, so having a market economy is not the only cause. China's fast economic growth can be partially attributed to that fact that the central government gave local governments the incentive to develop, so local governments became competitors. Wang stated that the central government now wants to strengthen its control again. The problem, as he sees it, is with the environment and natural resources, where protection is not necessarily aligned with interests in local development.

Central Government Funding Key to Sichuan Development

¶11. (C) Wang opined the central government should take an overall view of development in the country and enact better regulations in favor of the environment, energy efficiency, and peoples' livelihoods. He asserted the amount of funding being transferred to the western areas from the coastal region of China is only a percentage of local funding, and he thinks it is far from enough. While Wang noted that in some areas of the province, 80 to 90 percent of local funding comes from the central government, he still advocated more transfers. To accomplish higher transfers, Wang believes taxes should be raised to increase the fiscal income of the government. Further, he thinks taxes in coastal areas should be increased, and the revenues transferred to the west. Wang also argued for the adjustment of local government functions, including the provision of education in rural areas. He stated that every citizen needs basic public services, which depend on the economic power of the government, and concluded by wondering aloud how this could be accomplished now that agricultural taxes have decreased.

Problems Attracting Foreign Investment

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¶12. (C) Even though the investment environment has been "perfected" and conditions have improved, Sichuan is still ten years behind the coast, Wang stated. Several problems cannot be easily resolved. Due to the inland location, transportation infrastructure is underdeveloped. In addition, inland Chinese have fewer contacts with overseas Chinese than residents of coastal areas. Initially, much of the investment in China came from Hong Kong and Taiwan, because of close relationships with coastal communities on the mainland, Wang commented.

¶13. (C) In spite of the challenges, Sichuan does have the ability to attract enterprises from abroad and from coastal areas for a number of reasons:

- Labor costs are low;
- The transportation infrastructure has improved (air and roads);
- The technical infrastructure is strong (because of the

"third-line" industrial base from Mao Zedong's redistribution of industrial and technical resources inland to survive a nuclear attack from the former USSR);

- Sichuan is a hub for the Great Western Development Strategy; and
- There is a large market here.

Sichuan still needs a lot of foreign investment in order to develop modern management and administrative expertise, Wang stated. In the end, the province will be able to attract new companies because the investment base is still very low. Economic growth will be fast, he predicted.

¶13. (C) This report has been coordinated with INR visitors.
BOUGHNER